SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1916.

No. 744. 52

LINCOLN GAS & ELECTRIC LIGHT COMPANY,
Appellant,

vs.

THE CITY OF LINCOLN *et al.*,
Appellees.

Supplemental Brief of Appellant.

CHARLES A. FRUEAUFF,
Solicitor for Appellant.

DEWEY C. BAILEY, JR.,
ROBERT BURNS,
Of Counsel.

APPEAL PRINTING COMPANY, NEW YORK

IN THE

Supreme Court of the United States.

LINCOLN GAS & ELECTRIC LIGHT COMPANY, Appellant, *against* THE CITY OF LINCOLN *et al.*, Appellees.	No. 744.

SUPPLEMENTAL BRIEF OF APPELLANT.

POINT I.

Effect of Stipulation.

It has just been brought to our attention by telegraphic communication from local counsel in Lincoln that the appellees have set up in their brief in opposition to the petition for a bill of review (which at the time of the preparation of this brief, we have not had an opportunity to examine), the fact that a stipulation was entered into by the parties at the time the one dollar rate for gas was put into effect. This stipulation was entered into on approximately May 1st, 1915, at the time the one dollar rate was put into effect by Lincoln Gas and Electric Light Company.

We submit that this stipulation, construed in the light of the circumstances under which it was entered into, and the intention of the parties at

the time, has no bearing whatsoever upon the present petition of the company for leave to file a bill of review.

When the stipulation was entered into, the Master had filed his report containing his findings, but the report had not come before the District Court for hearing on the objections of the Company to the report, although it was expected that a hearing on the Master's report would be shortly held. As a matter of fact, this hearing on the Master's report was held in the following month, to wit, June, 1915.

The stipulation was entered into with the intention that the fact that the one dollar rate had been put into effect would not be taken to be an admission as an acceptance of or compliance with the ordinance of 1906; and furthermore, that neither party would bring to the attention of the Court upon the hearing on the Master's report the fact that the one dollar rate was then effective.

We submit that this intent clearly appears from the stipulation itself. It is entitled in the Court below, and reads, "The action of the Gas Company in establishing such new rate shall not be shown in evidence or presented to *the Court* in the above entitled cause, or used in any way by either party to influence the action of the Court in the disposition of the case involving the validity of said 1906 gas ordinance." "The Court" referred to in the stipulation was the District Court, and the particular proceeding which the parties had in mind in drawing up the stipulation was the hearing before the District Court on objections to the Master's report.

We submit that it is idle to now argue that this stipulation was intended to bind the com-

pany from ever showing the effect of this one dollar rate at any time in the future; because it is apparent that even if the decision of the Court below should be affirmed by the Supreme Court of the United States upon the hearing of the appeal, this Honorable Court would not dismiss the bill without prejudice, but in conformity with its established policy, would permit the company, at any time in the future, to bring further proceedings to test the compensatory character of the rate fixed by the ordinance after an actual trial and test of the rate showed what its effect was upon the company's earnings. These further proceedings would be supplementary to the present case, and its object would be to obtain an amendment at the foot of the decree modifying the decree to such extent as would be justified by the showing made after the actual trial and test of the rate. According to the construction now attempted to be put upon this stipulation by counsel for the City, it would seem that they are trying to prevent the company from ever raising the question of the actual operation of the rate ordinance. This is, we submit, clearly erroneous and quite foreign to the intention of the parties when the stipulation was entered into.

Confirming our view that the intention of this stipulation was merely to cover the hearing before the District Court on objections to the Master's report, we beg to point out that counsel for the City in the proceedings to determine the amount of the bond on appeal after the District Court had confirmed the Master's report, called the attention of the District Court to the fact that this one dollar rate had been put into effect and used this fact as one of the factors to be con-

sidered in determining the amount of the bond. At that time under date of November 17th, 1915, they wrote a letter to the Hon. Page Morris, who was considering the amount of the appeal bond, they said:

> "In addition to the matters submitted in the oral statement to Judge Elliott, one important element should be submitted, namely, while the company has voluntarily reduced its rate to approximately the rates prescribed by the ordinance, it is to be remembered that as a matter of law the ordinance is not recognized by the company, and in the event that the company should so desire they could advance the rates again any time they choose to the old figure of $1.20 in which event even a $600,000.00 bond would be wholly inadequate."

Counsel for the company at that time raised no objection to the mention of this matter by counsel for the City to the District Court, because it was so thoroughly in accordance with the view of the company's counsel that the stipulation was merely intended to affect the hearing on the objections to the Master's report; and we submit that the action of counsel for the City in bringing to the attention of the District Court at the time of fixing the amount of the appeal bond the fact that the one dollar rate had been placed into effect by the Company, shows conclusively that it was their construction of the stipulation that it was merely so intended to affect the hearing before the District Court on the objections to the Master's report.

This stipulation was entered into by local counsel at Lincoln on behalf of the company, and if this Honorable Court deems the matter of the

stipulation to be of such serious moment that it would affect the company's petition for leave to file a bill of review, we request that decision be left open until the company has an opportunity to file another brief prepared by local counsel who is thoroughly familiar with the circumstances surrounding the stipulation, in order that he may present fully his views in respect of this matter.

POINT II.

Bill of review or supplemental bill in the nature of a bill of review is the proper method of procedure in this case.

The Master found that while the ordinance rate would have been confiscatory at the time, he presumed there would be an increase in use of gas because of the reduction in rate. This point was, therefore, one of those in direct issue in the original proceedings, but the character of evidence which could then be produced was entirely speculative. However, now through the actual trial of the reduced rate, exact evidence can be produced which will rebutt the Master's presumption, therefore, this evidence is newly discovered and properly presentable through the medium of a bill of review or supplemental bill in the nature of a bill of review, and does not require the filing of a new bill or supplemental bill.

Respectfully submitted,
CHARLES A. FRUEAUFF,
Solicitor for Appellant.

DEWEY C. BAILEY, Jr.,
ROBERT BURNS,
Of Counsel.

IN THE

SUPREME COURT

OF THE

UNITED STATES

LINCOLN GAS & ELECTRIC LIGHT COMPANY,
APPELLANT,

V.

THE CITY OF LINCOLN, ET AL., APPELLEES.

SUPPLEMENTAL BRIEF OF APPELLANT.

Counsel for the City of Lincoln filed two supplements to their brief on the oral argument, and by the consent of the counsel on behalf of the City, this additional or supplemental brief is filed by the Company.

I.

THE MASTER'S VALUATION AS OF JANUARY 1, 1907.

The valuation of the Company's properties as of January 1, 1907, and the net earnings of the Company for the year 1907 are of first importance in testing the validity of the ordinance in question.

The Master found a total present value of $436,565.00 as of January 1, 1907, and found that the Company, at the $1.00 rate would earn 5.12 on that valuation for the year of 1907.

The valuation of $436,565.00 found by the Master includes (1), working capital, (2), going value, and (3), presumably twelve and one half per cent (12½%) over-head on the net construction cost as of January 1, 1907. It is impossible from the Master's findings to determine (1), the present value of the physical properties of the Company as of January 1, 1907, or (2), the reproduction cost of such properties, or (3), the amount of the accrued depreciation considered, and the depreciation by the Master from the replacement costs new to reach the present value, the basis employed by the Master in his valuation as of January 1, 1913. It is also impossible to determine from the Master's valuation of 1907 the amount included, (1), for working capital and (2), for going value, and (3), the amount of overhead expense added to the construction costs of the physical properties.

Judge W. H. Munger, upon the former hearing, found the replacement costs of the Company's properties excluded going value and interest during construction and certain other items of properties and values claimed by the Company, but included working capital of $50,000.00 in the amount of $616,073.59, and found the accrued depreciation to be $49,688.17, leaving the present value as of January 1, 1907, at $566,073.59 (Trans., p. 25). To this valuation so found by Judge Munger, should be added going value and interest during construction. With these two elements properly included in Judge Munger's valuation it will be seen that the Master's valuation for 1907 is approximately $200,000.00 below the figure fixed by Judge Munger.

The Company submitted a detailed valuation of the physical properties including working capital, upon the hearing before Judge Munger in the former trial, showing a valuation of $904,000.00 for the physical properties, including working capital, but excluding going value (Trans., p. 263). That testimony, as well as all testimony submitted to Judge Munger upon former trial was submitted to the Master.

The Company offered, upon the hearing before the Master, the testimony of Mr. Lea, whose testimony was largely the basis for the Master's findings, in the Des Moines Gas Case reviewed by this Court, showing a reproduction cost as of January 1, 1907 in the amount of $904,141.00 and a present value of $784,682.00.

The Master's lump sum figure for 1907 is clearly $200,000.00 below the then present value of the Company's properties as shown by the conclusive and overwhelming weight of the evidence and the net earnings of 5.12 per cent. upon such low valuation as fixed by the Master is clearly confiscatory.

TheMaster's valuation for 1907 utterly fails to comply with the order and direction of this court in the reversal of the case upon former hearings, to the effect that the Master should (1), report fully his findings upon all questions raised by either parties separately and that (2), he should make a full report upon the value of the properties, (3), the receipts and expenses of operation, (4), the sums paid out upon reconstruction and replacement, and the depreciation in past years and (5), a full report upon past depreciations, past expense for reconstruction and reproduction and past operating expenses, including current repairs. A lump sum valuation for 1907 of $436,565.00, including both tangible and intangible properties without any separation or segregation, and without any indication as to the amount of depreciation or the replacement costs new in the properties or any portion of the properties and without any findings as to how much the Company had expended for reconstruction or repairs prior to 1907, or how much the properties had depreciated at that time is a total and utter failure on the part of the Master to comply with the directions of this court.

The Company in its exceptions to the Master's report, pointed out specifically the above failure on the part of the Master (Exc. 1, Trans. p. 70). The Company also filed an application to recommit the case to the Master in order that specific findings should be made in the above matters (Request No. 17, Trans. p. 73).

Construction Account: The construction account of this Company shows a net amount of $784,307.49 at the close of the year of 1912, and $589,887.84 at the close of the year of 1906 (Trans. p. 1896).

The question was asked by Justice Brandeis on the oral argument as to whether the construction account showed the total investment of the Company undepreciated in 1912. The evidence referred to in the City's brief and also in our brief, page 100, shows that in case of replacements the new equipment taking the place of the old equipment was charged in the construction account with the difference between the cost of the new and the cost of the old, so by that process all completed depreciation was charged off, the new equipment by this method absorbed the depreciation in the old in the deduction in which it was charged in the construction account. The construction account to the extent of such completed depreciation does not reflect the total investment, but reflects the total investment less the total completed depreciation. The effect of deducting from the new equipment the original cost of the old is to charge the new equipment with all of the depreciation in the old. Further the evidence shows (Trans. pp. 2037-2061) deductions in addition to the deductions covering depreciation in the construction account as above indicated, further credits or deductions, in the amount of $59,754.15. These credits in the construction account have been deducted, leaving a balance in 1912 of $784,307.49, and at the close of 1906 the amount of $589,887.84. The construction account does not include working capital which the Master fixed at $60,000.00 in 1912 nor the twelve and one-half per cent overhead allowed by the Master, nor anything for going value.

II.

MASTER'S VALUATION FOR 1912.

With respect to the Master's 1912 values of $676,565.00 including working capital and going value, the difference between

the Master's present value on the physical properties including working capital and the present value of such properties as determined by Mr. Lea, exclusive of paving over mains and services is $68,859.00, as follows:

	Master.	Lea.	Difference.
Real Estate	$16,250.00	$18,350.00	$2,000.00
Buildings	29,381.00	30,967.00	1,586.00
Work Equipment	179,310.00	196,759.00	17,449.00
Distribution System	351,624.00	387,445.00	35,821.00
Working Capital	60,000.00	72,038.00	12,038.00
Total Difference			$68,859.00

The Master excluded from the value of the distribution system $30,484.00, representing payments made by consumers on house services, which is included, however, in Mr. Lea's figure and which if deducted from Mr. Lea's valuations would leave a net difference of $38,411.00 in the valuation of the physical properties, including working capital.

The error in the City's tabulation submitted at the close of the argument showing a net difference of $11,000.00 in the values of the physical properties results from deducting from the present value undepreciated, going value and overhead items in Lea's valuation, and by including and deducting as a separate item $33,000.00 organization expense which is a portion of Lea's overhead. By its deducting as a separate item, after deducting overhead, a double deduction for this item occurs.

III

THE MASTER'S 1912 OPERATING EXPENSES.

The Company complains of the Master's 1912 finding more particularly because of the deductions made by the Master in the operating expenses for 1912, amounting to $23,000.00, which represented money actually expended by the Company in the operation of its properties.

The exclusion of more than $7,000.00 from the operating expense in the new business department we believe was not justified and particularly in view of the fact that a large portion of the total expenditures of the new business department would be incurred by the Company necessarily if there was no new business department.

Expenditures of the Company in holding and getting business under serious competition on the part of the City should be considered with some degree of liberality in a contest with the City and the Company should have considerable latitude in the exercise of its judgment as to necessary expenditures to preserve, protect and extend its business, and should not be held to limitations or restrictions proposed by the City. The Master's restrictions on such expenditures would have been unnecessary in the absence of such competition since it is fair to assume that such expenditures would not have been incurred in the absence of competition. The Master we believe attached too much importance to the results in getting new business, and not enough importance to the efforts of the Company to hold old business. The Company would be doing well to hold its volume of business by such expenditures in view of the growth of the City of 4,000 in ten years, and in view of the aggressive competition on the part of the City and Traction Company in the electric field. The field for expansion by reason of the small increase in growth in City was very limited and the Company was doing well to hold its own even with the expenditures in the new business departments.

Further expenditures of the character in question would necessarily belong either to the operating expenses or capital account of the Company. They were either an operating expense or a capital investment. The Master excluded the amount so expended to the extent indicated in his report from both accounts. In this the Master clearly was in error.

An analysis of the new business department account is found in the record (Trans. pp. 1537-1559), showing that the expenditures charged to this department include portions of

the (1), rent, heat, lighting, telephone charges, (2), barn expenses, (3), labor expenses in connection with setting and resetting meters and connections and (4), rebates and allowances. The appliance account standing alone (Trans. pp. 1543-1551) shows a gain of more than $1,000.00 in 1912, and more than $5,000.00 in 1913 (Trans. p. 2062, Sub. G 15). The City's contention that the handling of appliances in 1912 was at a loss of $7,301.93 is reached by charging alone the appliance account with the expenditures of the new business department, which expenditures were incurred not in the sale of appliances alone, but in getting and holding business, including certain salaries for the new business department, wages, labor, advertising, etc. It is apparent that if the total expenses of the new business department is charged against the receipts from the sale of appliance which is only a subdivision of the new business department the profits on the appliance account would have to be sufficient to carry the total expenses of the new business department or a loss would be shown. A fair comparison would be to consider the appliance account standing alone showing the amount of money paid by the Company for the appliances purchased, and showing the amount of money realized upon appliances sold and the expenses involved in making the sale, and if the appliances were sold for more than the Company paid for them, plus such expenses, to the extent of such difference a profit would result from the handling of appliances which in turn could be used by the Company in defraying other expenses of the new business department.

In 1912 the expenditures of the Company to the extent of $19,692.64 were charged to the new business department. In 1913 this amount was reduced to $10,399.90. This reduction, however, was due in part to the fact that the sale of the appliances standing alone resulted in a profit of more than $5,000.00 (Trans. p. 2062, Sub. G 15). The sales of gas in Lincoln, however, dropped from 227,297 M. cu. ft. in 1912 to 220,000 M. cu. ft. in 1913.

The manager of the Company, found by the Master to be competent and skilled approved the expenditures of the Company charged to the new business department. The Master eliminated $7,692.64 of the $19,692.64 expended in the year of 1912 in that department. There is, we believe, no fair basis or justification for the elimination of $7,692.64 of the expense of the Company so incurred in 1912. The Master may as well have eliminated all of it as any part of it so far as having any basis in the record for his action is concerned.

The Master also eliminated an expenditure in 1912 of $3,000.00 paid the chairman of the board of directors, and $600.00 paid New York counsel, a total of $3,600.00. The total executive salaries of the Company, including president, vice-president, chairman of the board of directors, manager, secretary, assistant secretary and treasurer for the year 1912, chargeable to the gas department was $8,917.30. This expense was approved by the manager. There is no testimony in the record showing the amount to be excessive or unreasonable or unnecessary. The exhibits compiled from the Massachusetts companies show the total executive salaries to have been moderate and in fact low and there is nothing in the record to support the elimination or any part of it. We have already pointed out that the Master eliminated the whole of the particular salaries in question when only a portion was charged to the gas department, in which the Master clearly erred.

Electric Department General Expenses: The table set out in the City's brief, page 142, purporting to show the general expense in the electric department for the years 1903 to 1912 inclusive, is for the purpose of showing that certain expenditures of the Company in common between the gas and electric departments had increased in the gas department and decreased in the electric department. The Master found that certain expenses in common between the two departments should be apportioned on the basis of the relative number of consumers in the two departments.

The record shows that prior to April, 1908, the expenditures in question were apportioned and charged, fifty per cent. to the gas department and fifty per cent. to the electric department (Trans., pp. 137 and 769). But it developed upon the former trial that this apportionment of the common expenses should be readjusted upon the basis of the relative number of consumers in the two departments which at the time stood eighty per cent gas and twenty per cent electric. Prior to that time no particular attention had been given to the matter of proper division of these common expenses and too great a portion of such expenses were being charged to the electric department. The result of making the change in April, 1908, from a basis of one-half to the gas department and one-half to the electric department to eighty per cent. to the gas department and twenty per cent. to the electric department necessarily increased the amount charged to the gas department and decreased the amount charged to the electric department. The basis for charging these common expenses as made in April, 1908, was approved by the Master. The net result of the table set out in the City's brief is to show the decrease in the electric department between 1908 and 1912, which at first thought appears important but with the fact in view that the decrease was due to a readjustment between the two departments on a proper basis, the result is neither important nor unexpected.

With respect to the increase of the expenditures of the legal department referred to in the City's brief, it should be borne in mind that all claims such as personal injury claims or claims on account of injuries to property were charged to this department (Trans. p. 163).

The evidence shows that in 1907, $1500.00 of a personal injury judgment was charged to the account of legal expenses (Trans. pp. 163 and 2062, Sub. G 14), and in 1913 settlements in the amount of $2200.00 were charged to this account; in other words it is an acocunt that does not represent simply the

salaries paid for legal services, and in so far as it represents settlements or judgments against the Company neither the increase nor the decrease of the amount could be controlled by a rate ordinance. The evidence shows that in 1906 the total legal expenses in this account chargeable to the gas department was $757.43 (Trans., p. 1386, Sub. 483), while in 1907 the amount was $2,160.31 (Trans., p. 1386, Sub. 487), and in 1912 it was $7,954.73 (Trans., p. 1386, Sub. 492). The evidence shows important litigation outside of personal injury suits, claims and settlements and outside of this gas rate ordinance. The Company has pending a suit brought on behalf of the City of Lincoln to terminate its right to do business and to furnish gas at any price, claiming that the Company's franchise has expired. Such a suit is of great importance to the Company and involves practically the total investment of the Company, and the Company would necessarily be required to pay for the services of competent counsel. The City also brought suits against the Company involving occupation taxes in which judgments were recovered against the Company in the amount of something over $80,000.00, which were appealed to the Supreme Court by the Company and presented there with the results as indicated by the City in its brief. The record shows that the expenses of the preparation and hearing before the Master on this rate ordinance are not a part of the expenses involved in any of the years from 1907 to 1912, inclusive, but that a special account carrying all such expenses was opened January 1, 1913 (Trans., p. 1559) so that such expenditure are not involved in the expenditures considered by the Master in his 1912 valuation or his 1907 valuation.

Working Capital: It is argued in the City's brief that the Master allowed too much working capital and that the proper amount would be represented by the average monthly pay-rolls plus the average monthly vouchers. The argument being that if the total amount paid for labor and material,

including supplies, for twelve months should be divided by twelve the result would represent the necessary working capital.

The record shows that the Company was required and did keep on hand a large amount of supplies ($16,000, Trans. p. 1300), including pipe, meters, etc., and also was required and did keep on hand a large amount of coke and coal and oil. The record shows that in 1907 at the time the inventory was taken the Company had on hand more than three thousand tons of coal. It was necessary that the Company protect itself at all times against traffic conditions, weather conditions and trade conditions and was obliged to keep ample supplies of all of its materials on hand so that in case of temporary delays or shortage from any cause, the Company could go on for a considerable period and serve the public. The City's basis of determining the working capital would limit the Company to the amount necessary for one month and where the Company had three thousand tons of coal on hand the City would consider only that part on hand as a part of the working capital which would represent the average monthly consumption of coal for the year, which would not represent the amount the Company had invested in coal and had on hand during any of that time, but would represent about one-third or one-fourth of it.

Depreciation: It is argued in the City's brief that Mr. Lea presented the sinking fund method of taking care of the depreciation for the purpose of gaining some advantage for the Company in this case. The fact is that the City on the former hearing presented Professor Beemis as its expert, who came into the case for the purpose of advocating for the City the sinking fund method of determining and providing for depreciation (Trans., p. 217). The Company through Mr. Lea's testimony presented in detail throughout the valuation of the Company's property both the straight

line depreciation and the sinking fund annuity (Trans. p. 1304, Sub. 1 to 22). The two methods are completely and definitely set out in Mr. Lea's valuation. Depreciation is an operating expense and the Company took the position that if the straight line method was employed then it would be necessary to provide a larger amount in operating expenses to take care of it than if the sinking fund method was employed and we were indifferent as to which method was used. The operating expenses would be increased or decreased according to the amount of the depreciation. The City first used the sinking fund method and urged its adoption (Trans. p. —) on the former hearing and before this Court as is shown by a reference to the brief presented to this Court by the City, but later upon the hearing before the Master adopted the straight line method. Its expert witness applied the straight line method of depreciation to the physical property, assuming a life and accepting the Company's statement for the ages of the property so far as past depreciation was concerned, but as to future depreciation and for the years of 1907 to 1912 attempted to measure it by a certain number of cents per thousand feet of gas sold, which method the Master found to be improper, bearing no direct relation to the subject of depreciation. It is evident that neither the straight line method nor the sinking fund method can be properly applied without qualification to past depreciation in reaching present value. Either the straight line method or the sinking fund method would be proper in measuring past depreciation in so far as it applies to service value. Either method would be proper in measuring depreciation in the future, because you have an established value, which represents the actual present value, and we assume that the actual present value less depreciation will continue during the time the prescribed rate based upon that value continues. But as to past depreciation either method cannot be applied without qualification. If we assume the water gas set has a life of twenty years, and was purchased ten years ago at a cost of $20,000.00 and would cost

new at this time $10,000.00, applying the straight line method of depreciation to the present cost, we would have a result of $5,000.00, whereas if applied upon a rate fixed at the time the equipment was purchased, we would have a value of $10,000. If the same water gas set ten years ago cost $10,000.00 and has a life of twenty years, and at this time would cost $20,000.00, then by the application of the straight line method of depreciation the present value would be $10,000. The straight line method or the sinking fund method in measuring future depreciation assumes because the rate is established on the present value, that the rate will continue in effect as long as the present value continues less the depreciation and for that reason may be properly applied to future depreciation, but the courts and commissions in determining past depreciation accrued prior to the rate in question determine the actual depreciation, not theoretical depreciation. Judge Munger upon the former hearing found that the property in 1907 as a whole had depreciated in the amount of $49,688.17 which was ten per cent of the value of physical property new exclusive of real estate and working capital. This $49,688.17 did not represent either the straight line or the sinking fund depreciation but represented the actual accrued depreciation as found by the court.

The amount of the depreciation should not fluctuate with market changes in the cost of equipment, but rather should measure the exhaustion in the equipment which should be compensated for in the operating expenses for depreciation based upon the original investment so that the original investment will remain unimpaired. The Company's property revalued as today would probably be fifty per cent greater than the valuation as of January 1, 1913, with depreciation deducted for the four years intervening because of the advances in the cost new equipment. The City valued the Company's gas mains in 1912 from $24.00 to $26.00 per ton and applied the straight line depreciation for the time the mains had been in use to the $24.00 to $26.00 per ton whereas

the mains cost the Company from $30.00 to $36.00 per ton and if the straight line depreciation had been applied to the $30.00 to $36.00 per ton, a much higher present value would have resulted. The cost at this time would probably be from $40.00 to $50.00 per ton and if the straight line depreciation was applied to that value covering the time the mains had been in use, the result would approximate the original cost notwithstanding the depreciation. The original investment when properly and fairly made should not be subjected to impairment by such radical changes as have occurred in the market value of equipment by making such market value the basis for the application of either the straight line or sinking fund depreciation without some qualification.

IV.

VALUATION AND RATE OF RETURN FOR THE YEARS 1907 TO 1912 INCLUSIVE.

The sales in 1912 in cu. ft. were 227,297 M. cu. ft. The actual operating expense with depreciation added as determined by Mr. Lea and exclusive of the occupation tax was $197,277. From this total operating expense the Master made the following deductions:

1. The expense of the new business department for the year 1912 was $19,692.64. The Master allowed $12,000.00 for this item of expense actually incurred by the Company or a reduction of $7,962.64 from the $197,277.00 total operating expenses, including depreciation.

2. The Master deducted $3,300.00 because of expenditures of the Company in common between the electric department and the gas department wherein certain expenditures in common were apportioned between the gas department and the electric department on the basis of eighty per cent to the gas department and twenty per cent to the electric department. The Master apportioned these expenses on the basis of seventy-three per cent to the gas department, and twenty-seven per

cent to the electric department, resulting in a deduction of $3,300.00. The number of consumers in the two departments varied somewhat from year to year, and in 1907 stood in a ratio of eighty per cent gas and twenty per cent electric consumers, and for the ten years 1902 to 1912 inclusive, the average was seventy-nine per cent gas and twenty-one per cent electric, which we assume to be the fair basis of apportioning the common expenses (Trans. p. 1849). If the seven per cent deduction resulted in $3,300.00 then one per cent would result in one-seventh of that amount or $471.42 and the one per cent would represent the difference between eighty per cent and twenty per cent and seventy-nine per cent and twenty-one per cent so that the deduction in any event should not have been for more than $471.42 in place of $3,300.00.

It is evident the Master considered the common expense which he apportioned on the basis of seventy-three per cent to the gas and twenty-seven per cent to the electric departments in the amount of $47,142.00 upon which amount seven per cent reduction would result in $3,300.00. It is impossible to determine from the report or the record what constitutes the $47,142.00 of common expenses.

In 1907 the common expense was apportioned on the basis of fifty per cent electric department and fifty percent gas department, but the Master made no correction in the apportionment for 1907 and in this his report was clearly in error if his basis for apportionment was correct in 1912. And had the correction been made by the Master, the common expense in 1907 would have been increased in the gas department thirty per cent, which would have decreased the net earnings $14,142.60 and would have reduced the Master's net earnings for that year from $27,179.00 with the occupation tax eliminated to $13,036.40 considering the common expense in the amount of $47,142.00 assumed by the Master in 1912, and would have rseulted in the net earnings on the Mas-

ter's valuation of 2.7%. If it was proper for the Master in 1912 to apportion the common expense upon the basis of the relative number of consumers in the gas and electric departments then there could be no escape from the necessity for making the same apportionment in 1907 on the same basis notwithstanding it would result to the disadvantage of the City.

3. The Master deducted $3,600.00 covering the salaries of Mr. Henry L. Doherty and Mr. Charles A. Frueauff, representing the total amount for the year 1912 paid to Mr. Doherty and Mr. Frueauff. The total amount in any event should not have been deducted by only seventy-nine per cent thereof or $2,884.00.

4. Mr. Lea included in the $197,277.00 depreciation in the amount of $20,865.03. The Master allowed for depreciation in 1912, $12,000.00 which would result in a deduction of $8,865.03 bringing the total operating expense down to $177,314.33.

5. To the $177,314.33 should be added the occupation tax of three per cent on $227,297.00 at the $1.00 rate, or $6,818.91, which results in a total operating expense on the Master's basis with the corrections in his figures, as above indicated, $184,128.24, leaving the net earnings for 1912 at $43,169.00. The Master in making the computation by reason of the errors above noted, reached the figure of $46,658.00. The errors, however, are apparent.

The Master does not give the value of property for any of the intervening years between 1907 and 1912, and so far as the operating expenses are concerned gives only the amounts for such years as shown by the Company without any definite deductions, so that no exact figure can be made of the net earnings for such intervening years. However, the Master found that the total depreciated value of the property added between the years 1907 to 1912 inclusive, was $240,000.00.

The construction account (Trans. p. 1896) shows the total construction for 1907 in the gas department to have been

$16,017.70; for 1908, $73,638.84; for 1909, $23,031.93; for 1910, $50,248.06; for 1911, $20,033.10! for 1912, $27,167.72, which is exclusive of the $30,484.43 paid on house service by consumers during said period (Trans. p. 1826).

In view of these expenditures shown in the construction account and in the absence of any findings of value, by the Master for the intervening years, it is necessary to assume an apportionment of the $240,000.00 added depreciated value for the years covered by the expenditures. For the purposes of the calculations which are here submitted we have apportioned the $240,000.00 equally between the six years, 1907 to 1912, being $40,000.00 for each year. If the $40,000.00 is deducted from the valuation found by the Master at the close of the year of 1912 and $10,000.00 added covering the depreciation on the property for that year exclusive of the $240,000.00 depreciated value added between 1907-1912 inclusive, we would reach approximately the Master's value of the property at the beginning of the year of 1912 before the $40,000.00 additional depreciated value had been added and before the $10,000.00 depreciation had been taken off and by the same process working back to 1907 we can reach approximately a value for each of the years on the Master's basis of valuations for the year 1912.

The operating expenses for the intervening years we must necessarily assume to be the amount actually expended by the Company as we have no deductions by the Master except for the year 1912, the 1907 operating expenses being allowed by the Master as reported by the Company. The 1913 operating expenses were offered in evidence as shown in Exhibit "424," page 2060, and the new construction in 1913 more than offset the depreciations so that it is altogether fair to the City to assume the present depreciated value in 1913 the same as found by the Master in 1912. The table below shows the valuation, net earnings and per cent of net earnings on the valuation for each of the years 1907 to 1912 inclusive, prepared as above stated.

MASTER'S VALUATIONS.

1.

Master's Valuation as indicated above not including the $100,000.00 of going value found by Master but excluded.

Year	Valuation	Actual Net Earnings	Per Cent.
1913	$676,567	$23,791	3.4%
1912	676,565	23,257	2.4%
1911	646,565	35,309	5.4%
1910	616,565	39,569	6.4%
1909	586,565	51,076	8.7%
1908	556,565	41,982	7.5%
1907	496,565	27,179	5.4%

2.

Master's Valuation including the $100,000 of going value found by Master, but excluded.

Year	Valuation	Actual Net Earnings	Per Cent.
1913	$776,567	$23,791	3. %
1912	776,567	23,257	2.9%
1911	746,565	353,091	4.7%
1910	716,565	39,569	5.5%
1909	686,565	51,076	7,4%
1908	656,565	41,982	6.3%
1907	596,565	27,179	4.5%

LEA'S VALUATION.

Year	Valuation	Actual Net Earnings	Per Cent.
1913	$1,090,913	$23,791	2.1%
1912	1,090,913	23,257	2.1%
1911	1,051,172	35,309	3.3%
1910	985,878	395,690	4. %
1909	926,712	51,076	5.5%
1908	830,120	41,982	5. %
1907	784,682	27,179	3.4%

The two and one-half occupation tax under the ordinance for the years 1907, 1908, and 1909, has been excluded from the operating expenses in the above table. The occupation tax of three per cent for the years of 1910, 1911 and 1912, at the one dollar rate has been included as the case involving the validity of that ordinance is awaiting a determination of the rate in order to fix the amount on which to compute it.

The average for the period according to the Master's findings as above in tabulation one would be 5.7%, and in tabulation two would be 4.9% and the average for the period as shown by the Company's valuation and its actual operating expenses would be 3.6%.

The evidence shows that in 1904 the Company was struggling to get money for its operating expenses and for extensions and betterments on its 7% notes secured by double the amount of the notes in bonds plus 2% commission on the notes and was unable to get money on that basis and the stockholders advanced $100,000.00. The rate of gas in Lincoln about that time had been reduced 30c per thousand. The evidence shows that in 1909 the Company's first mortgage bonds in the amount of $333,000.00 would mature the following year and the Company, in order to get the money to take up said bonds, was obliged to issue short time 6% notes, for which the bonds were held as collateral secured by a first mortgage in the amount of $333,000.00 on the combined properties of the gas and electric departments. On that basis it was necessary for the Company to suffer a discount and the notes were sold under the order of the Railway Commission on the basis of 96c on the $1.00 resulting in an interest charge of 7.6%. The evidence also shows that when those notes matured it was necessary for the Company to take them up by another note issue under like conditions. It is absurd to say that a fair rate of return upon investment in the properties would be 5% or 6% in face of the fact that in financing the Company's needs for money where the security was a first mortgage lien limited to

$333,000.00 on the combined properties of the gas and electric departments, the Company was obliged to pay 7.6%. If the Company was obliged to pay 7.6% for money to maintain its business and properties and for betterments and extensions in 1909 to 1912 a rate or return short of that amount would be confiscatory, because it would not be a fair rate of return determined by the actual experience of the Company.

In conclusion we want to again urge upon the attention of the court that enforcement of the ordinance against the Company would result in confiscation of practically the entire property of the Company. The 20 cents per thousand refund with interest amounts to approximately $525,000.00. The entire earnings of the property between the years 1907 and 1912 were devoted to (1) payment of bond interest and, (2) the maintenance and operation of the property. The application to the Railway Commission for permission to issue the $500,000.00 of notes shows that the difference between the $333,000.00 of bonds retired and the $500,000.00 was to cover money furnished for extensions and betterments in the property. The Master's valuation as of January 1, 1913, was $676,565.00. In this situation the confiscatory character of the rate ordinance in question appears to be clearly and conclusively demonstrated.

Respectfully submitted,

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